No. 889

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1955

O. HENRY BRIGGS, THOMAS J. DEEGAN, JR., WALTER W. FOSKETT, HENRY J. GUILD, ALLAN P. KIRBY, HERMAN R. NEFF, ROBERT R. YOUNG, CLINT W. MURCHISON, SID W. RICHARDSON, JOHN D. MURCHISON, CLINT W. MURCHISON, JR., MURCHISON BROTHERS and ALLEGHANY CORPORATION,

Petitioners,

v.

BRESWICK & CO. and MYRON NEISLOSS, as stockholders of Alleghany Corporation and on behalf of themselves and all other stockholders similarly situated,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners pray that a writ of certiorari issue to review an order of the United States Court of Appeals for the Second Circuit which dismissed petitioners' appeal from a District Court injunction on the ground that the order was "interlocutory." The Court of Appeals so acted in the face of Sections 1291 and 1292 of the Judicial Code, which permit appeals from both final and interlocutory injunctions.

Citations to Opinions Below

The opinion of the District Court, per Walsh, J., printed in Appendix B *infra*, p. 1, is reported in 135 F. Supp. 397. The memorandum decision of the Court of Appeals, printed in Appendix B, *infra*, p. 22, is unreported.

Jurisdiction

The order of the Circuit Court of Appeals was entered on January 23, 1956, Appendix B, *infra*, p. 23. The jurisdiction of this Court is invoked under Section 1254(1) of the Judicial Code. 28 U.S.C.A. Sec. 1254(1).

Question Presented

Whether an appeal will lie from an order of the District Court permanently enjoining defendants in a derivative stockholders suit from pleading as a defense a proposed judgment which may be rendered in a State Court action on the same derivative causes of action.

Statutes Involved

The statutory provisions involved are Sections 1291, 1292(1), 1738 and 2283 of the Judicial Code. They are printed in Appendix A, *infra*.

Statement

On February 14, 1955, respondents commenced the present stockholders' derivative suit in the United States District Court for the Southern District of New York against Alleghany Corporation and the individual petitioners, directors of the Corporation and their alleged co-conspirators. The complaint alleges waste of corporate assets, appropriation of corporate business opportunities, and a conspiracy to violate the Investment Company Act of 1940, 15 U.S.C.A. Sec. 80a-1, et seq. Jurisdiction of the District Court is invoked as to Counts 1-4 under Section 44 of the Investment Company Act, 15 U.S.C.A. Sec. 80a-43, and as to Counts 5-7 under Section 1332 of the Judicial Code,

28 U.S.C.A. Sec. 1332 (diversity of citizenship; amount in controversy over $3,000).

On October 27, 1955 the District Court issued an order "permanently enjoining" petitioners, defendants there, from pleading as a defense in this action any judgment of dismissal which might be rendered, pursuant to a proposed settlement, in an action pending in the Supreme Court of the State of New York. Appendix B, *infra*, p. 18. The complaint in the State Court action alleged, among others, all of the causes of action alleged in the present complaint. Petitioners appealed, and on respondents' motion the Court of Appeals for the Second Circuit summarily dismissed the appeal on the ground that the order was "interlocutory." Petitioners ask this Court to direct the Court of Appeals for the Second Circuit to hear their appeal from the injunction issued in the District Court.

To appreciate the significance of the extraordinary injunction issued by the District Court and the collision between the lower federal and state courts which will result if prompt review of the injunction is denied to petitioners, it is necessary to have a fuller picture of the facts.

The present action is one of over twenty derivative stockholder suits against the directors of Alleghany Corporation, including the present petitioners, growing out of the New York Central proxy fight of 1954. See Appendix B, *infra*, p. 2, et seq.

The first of the related derivative actions was brought in the District Court in April of 1954 by one Sadie Zenn, represented by Pomerantz, Levy & Haudek. At about the same time, similar actions were brought in the Supreme Court, New York County. The usual deluge of overlapping stockholders' actions ensued.

In May of 1954 all pending stockholders' actions in the District Court were consolidated ("the Federal Court Zenn action"). Shortly thereafter a similar consolidation order was entered in the State Court ("the State Court Zenn action"). In each court the firm of Pomerantz, Levy & Haudek was designated general counsel for the plaintiffs. They thereupon commenced depositions and other pre-trial proceedings.

Eight months after these earlier suits were consolidated the instant action (twenty-second in the series) was brought, the complaint copying some but not all of the causes of action in the Zenn complaints.

In April of 1955 a proposed settlement of all the interrelated derivative claims (subject to court approval) was agreed to between petitioners and Pomerantz, Levy & Haudek, the court-appointed general counsel for the stockholders in the consolidated Zenn actions. This proposed settlement, whereby petitioners agreed to pay over to the Corporation approximately one million dollars in cash and guarantees, was publicly announced on July 25, 1955 and was thereupon submitted for approval to the Supreme Court of the State of New York, County of New York. That Court, on August 18, 1955, appointed a referee to hear and report. Notice was sent to all shareholders of Alleghany Corporation on whose behalf the action was brought, and they were invited to make any objection which they might have to the proposed settlement at the hearings to be conducted before the referee. If the State Court should approve the settlement, a judgment dismissing the State Court Zenn action would result and the individual petitioners would be awarded a judicially approved release from all liability to the Corporation on all of the derivative causes of action pleaded in any of the complaints.

On August 11, 1955, however, respondents herein moved in the District Court for an order enjoining the State Court proceedings, alleging that the settlement had been collusively negotiated. The District Court observed that it had no power to stay the State Court proceedings and further found that there had been no collusion in the negotiation of the settlement. Appendix B, pp. 9, 13. The District Court went on, however, to introduce a startling innovation into the law of res judicata. It held that respondents had a right to participate in the settlement negotiations alongside general counsel; that the failure to include them in the negotiations was inequitable; and that respondents' rights would not be sufficiently protected by their opportunity (of which they have since availed themselves) to be heard in

the State Court proceedings to determine the fairness and equitability of the proposed settlement. The District Court accordingly granted alternative relief, neither requested nor suggested at the argument, permanently enjoining petitioners from pleading any judgment entered in the State Court settlement proceedings as a defense in the present action.

From the order of the District Court entered October 27, 1955, defendants-petitioners appealed to the Court of Appeals. Upon respondents' motion, this appeal was summarily dismissed. It is the summary dismissal of this appeal which petitioners ask this Court to review.

Reasons for Granting the Writ

I.

The Court of Appeals dismissed the appeal on the ground that the District Court's order was "interlocutory." But Section 1292(1) expressly permits appeals from "interlocutory orders of the district courts of the United States . . . granting, continuing, modifying, refusing or dissolving injunctions. . ." See Appendix A, *infra*, p. 1. "Thus by the plain words of § 129 [the predecessor of Section 1292(1)] the Circuit Court of Appeals was authorized to consider the appeals from the temporary injunction." *Deckert* v. *Independence Shares Corp.*, 311 U. S. 282, 287 (1940). By dismissing petitioners' appeal from an injunction on the ground that it was interlocutory, the Court of Appeals "has so far departed from the accepted and usual course of judicial proceedings . . . as to call for an exercise of this court's power of supervision." Rule 19(1)(b) of this Court.

II.

Respondents contended below that the District Court's order was not actually an injunction or that, at least, the injunction was "surplusage." The argument, whether or not it was accepted by the Court of Appeals, would make a mockery of Section 1292.

The District Court's order expressly recites that the Court was *"permanently enjoining"* petitioners from pleading res judicata. Appendix B, *infra*, p. 18. If petitioners should plead as res judicata in this action a judgment issued in the State Court settlement proceedings, they would surely be in contempt of court. There can be no more conclusive criterion to demonstrate the injunctive nature of the order of the District Court.

The District Court's order recites "the reasons for the issuance of this injunction" (Appendix B, *infra*, p. 19) and otherwise conforms to the provisions of Rule 65 of the Federal Rules of Civil Procedure regarding the form and scope of injunctions. The District Court's intention to issue an injunction could not have been more clearly expressed.

The District Court's opinion characterized its order as "the equivalent of staying the execution of a judgment in the hands of a plaintiff without invalidating the judgment." Appendix B, *infra*, p. 11. An injunction against the enforcement of a judgment which the court deems inequitable is a traditional exercise of the Chancellor's power. See *Marine Ins. Co.* v. *Hodgson*, 7 Cranch [U. S.] 331 (1813); *Cage* v. *Cassidy*, 23 How. [U. S.] 109 (1859); 4 *Pomeroy's Equity Jurisprudence*, Sec. 1364 (5th Ed., 1941). The authorities which the District Court cited in support of its power to issue the injunction are all cases of clearly equitable injunctions. E.g., *Wells Fargo & Co.* v. *Taylor*, 254 U. S. 175 (1920).

Respondents contended below that the District Court's order was not in substance an injunction because it amounted to nothing more than the striking of an affirmative defense or a statement of intention to strike a defense. But no defense had been pleaded; and if the District Court had merely volunteered an opinion on a hypothetical state of facts neither the parties nor other judges of the District Court would have been bound. The District Court obviously felt that to achieve its end it was necessary to do more than merely to express an opinion. For the District Court recognized that the judgment once pleaded would be res judicata. Appendix B, *infra*, pp. 10-11; *Stella* v. *Kaiser*,

218 F. 2d 64 (2d Cir. 1954); *Dana* v. *Morgan*, 232 Fed. 85 (2d Cir. 1916). Thus a motion to strike the affirmative defense of *res judicata* would have to be denied. But the District Court held that the procedural device it adopted was proper because "[t]he sole thrust of this determination is against the persons of the defendants . . ." (Appendix B, *infra*, p. 11) plainly a result which could be attained only by the issuance of an equitable injunction. Petitioners are thus barred, on pain of contempt, from pleading a defense of res judicata which, if pleaded, admittedly must prevail. There is no procedural device other than an injunction by which this result could be reached.

III.

The District Court's order is an injunction in substance as well as form for another reason which brings this case within an area of particular concern to this Court—the area of federal-state relations. The District Court, mindful of the prohibitions in Section 2283 of the Judicial Code (Appendix A, *infra* p. 2), disclaimed any intention to enjoin the prosecution of the settlement hearings in the State Court. But the order actually issued—an injunction against the use of the State Court judgment—has practically the same effect. For it deprives that Court of the power to issue a judgment and authorize a release which will effectively terminate the complex litigation of which the case at bar is a part. Avoidance of the burden of litigation is, of course, a principal purpose of the parties in settling. Any distinction between tying the State Court's hands and pulling its teeth is mere formalism. If the District Court's order stands, it will deprive the State Court of the power effectively to exercise its admitted jurisdiction to pass upon and approve the proposed settlement.

Nor is this all. In practical effect the District Court's order may well force petitioners to abandon the proposed settlement, since they can hardly be expected to pay $1,000,000 in the State Court for the privilege of continuing to litigate the identical causes of action in the District

Court. This is doubly true when petitioners know that, if successful on the trial in the Federal Court, they will be unable to recoup the consideration earlier paid in settlement. In both aspects of the matter the District Court's injunction intrudes upon the power of the State Court to pass upon and approve a settlement which it may hold to be highly beneficial to the Corporation.

(If, in passing upon the question of appealability, this Court should hold that the District Court's order is an injunction for the reason, among others, that it throttles the State Court, this Court's opinion will incidentally have given assistance to the Court below in determining the merits of the appeal. For Section 2283 of the Judicial Code, prohibits federal courts from enjoining state court proceedings. "Certainly the injunction issued by the district court nullified defendants' efforts in the state court almost as effectively as would the injunction against state court proceedings which is literally proscribed by 2283." Note, 65 Yale L. J. 543, 548.*)

Timing is of the essence here, for if prompt review is denied in the federal courts and the result is an abandonment of the State Court settlement, the damage to the harmonious working of the federal-state relationship will have been done, the District Court's order will become moot, and neither the Court of Appeals nor this Court will ever have an opportunity to pass upon the propriety of the novel injunction which has been issued. Thus the question of reviewability goes to the heart of the federal-state problem here.

IV.

In the Court below respondents invoked cases such as *Morgantown* v. *Royal Insurance Co.*, 337 U. S. 254 (1949),

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* An extensive Note on this case in 65 Yale L. J. 543 (1956) disapproves the action of the District Court, both as an improper invasion of the State Court's jurisdiction (at pp. 547-48) and as establishing an unsound rule regarding the proper procedure for settling stockholders' derivative actions (at p. 550). The Note comments in passing that the denial of review by the Court of Appeals is "at least dubious" (fn. 47, at p. 549).

and *Baltimore Contractors* v. *Bodinger*, 348 U. S. 176 (1955), which held that the District Court orders there involved were not injunctions and therefore not appealable. But there exists no analogy between those cases and that at bar.

The District Court orders involved in *Morgantown* and in *Bodinger* did not purport to be injunctions. In *Morgantown* the District Court had denied a demand for a jury trial. In *Bodinger* the District Court had denied a stay of the action pending arbitration. In neither case did the District Court enjoin a party from doing or omitting anything. In neither case was a party subjected to the threat of contempt penalties for disobeying the mandate of the District Court. In the present case the District Court did issue an injunction and did subject petitioners to contempt sanctions.

The problem in *Morgantown* and in *Bodinger* was whether a District Court order, non-injunctive in form, should nevertheless be treated as an injunction for appeal purposes. Somewhat similar orders had been so treated in *Enelow* v. *New York Life Ins. Co.*, 293 U. S. 379 (1935), in *Shanferoke Coal & Supply Corp.* v. *Westchester Service Corp.*, 293 U. S. 449 (1935), and in *Ettelson* v. *Metropolitan Life Insurance Co.*, 317 U. S. 188 (1942). This Court had held in these earlier cases that the District Court's denial of a jury trial (in *Enelow* and in *Ettelson*) and the District Court's denial of a stay pending arbitration (in *Shanferoke*) were appealable because they granted relief which, prior to the merger of law and equity, could have been granted only by injunction. These historical reasons did not apply to the District Court orders in *Morgantown* and *Bodinger*; these orders were therefore treated as what they purported to be—namely, orders of the District Court regulating procedural matters in the cases before them.

The problems confronting this Court in the line of cases running from *Enelow* to *Bodinger* are not presented in the case at bar. We do not have here the question whether Section 1292(1) should, for historical reasons, be expanded beyond its literal terms. The District Court's order here is expressly denominated an injunction. It expressly re-

strains petitioners from engaging in specified conduct. It subjects petitioners to the jeopardy of a contempt punishment if they should disobey the Court's order.

It follows from what has been said above that, even if the decisions under discussion were in some fashion relevant to the case at bar, the District Court's order here would in any event be appealable. For, as shown in Points II and III, *supra*, that order is an exercise of a traditional equity power and it achieves a result not attainable except by injunction. It is therefore truly an equitable injunction not only in form but in substance as well.

V.

Respondents argued in the Court below that the appeal was premature because the State Court has not yet rendered a judgment approving the settlement. The argument is clearly unfounded. The fact that the State Court judgment has not yet been rendered might have been an additional ground for refusing to issue an injunction. But once the injunction was issued, the time to appeal therefrom was thirty days. Had petitioners waited beyond that period their appeal would certainly have been dismissed on the ground that it was not timely.

Respondents seem to suggest that petitioners should wait for the rendition of the State Court judgment, should then move to vacate the District Court's injunction and, upon denial of that motion, should then take their appeal. But under § 1292(1) an interlocutory injunction is immediately appealable regardless of the possibility that, at some future time, the District Court might vacate it. Moreover, the suggested motion to vacate the injunction would, in effect, be no more than an attempt to reargue the injunction which already in terms anticipates the issuance of the State Court judgment. It is well settled that the denial of such a motion is not appealable. *Marine Midland Trust Co.* v. *Eybro Corp.*, 58 F. 2d 165, 167-8 (C. A. 2, 1932).

VI.

The dismissal of petitioners' appeal by the Court of Appeals is not only in direct conflict with § 1292, it is equally contrary to § 1291, as construed in *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U. S. 541 (1949).

In *Cohen*, this Court held that *an interlocutory order* denying security for costs was appealable as *a final decision* under Section 1291 of the Judicial Code. Appendix A, *infra*, p. 1.* Justice Jackson, speaking for the Court, pointed out that:

> "This decision appears to fall in that small class which finally determine claims of right separable from, and collateral to, rights asserted in the action, too important to be denied review and too independent of the cause itself to require that appellate consideration be deferred until the whole case is adjudicated." 337 U. S. 541, 546.

The order of the District Court in the present action falls within that group of decisions described by Justice Jackson as final decisions within the contemplation of Section 1291. It is too important to be denied review in that it will, if allowed to stand, vitiate the settlement designed to put and end to the complex litigation of which this case is a part; and it will completely nullify the long and exhaustive proceedings conducted by the New York Court to determine the fairness of that settlement.

Further, the propriety of that order, as in the *Cohen* case, may be determined wholly apart from the questions involved in the underlying causes of action. The questions

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* That the Court of Appeals gave inadequate consideration to the question of appealability is strongly suggested by the following. Along with the appeal from the injunction order here in question, petitioners brought a companion appeal from a second order of the District Court denying security for costs on four causes of action. The court below dismissed the appeal from the latter order on the ground that it, too, was "interlocutory," a result flatly contrary to the *Cohen* case, on which we relied below. (The security for costs order appears in the present record, although it is not the subject of the present petition.)

of the conduct of the negotiations leading to the settlement, of comity, and of full faith and credit which must be considered on appeal from the District Court's injunction are entirely independent of any issues raised by the derivative claims asserted in the complaint.

VII.

Finally, we respectfully submit that the nature and importance of the questions denied review by the Court of Appeals may properly be considered by this Court in passing upon the present petition for a writ of certiorari. Two questions of far-reaching importance to the working of our dual system of courts are involved and deserve brief mention here.

We have already seen that the question of appealability leads to a consideration of the impact of the District Court's order on the State Court settlement proceedings. It is plain from the opinion of the District Court that the unique injunction involved here was resorted to because it appeared that a direct injunction against the State Court settlement proceedings would be prohibited by Section 2283. Yet the effect of the injunction, as noted above, would be precisely to nullify those State Court proceedings, since defendants could not be expected to pay $1,000,000 to the corporation merely for the privilege of continuing litigation in another court. The District Court has simply done indirectly that which it could not do directly. Such attempts at circumvention have been sharply disapproved by this Court in its most recent decision construing Section 2283:

> "By that enactment [the 1948 amendment to Section 2283] Congress made clear beyond cavil that the prohibition is not to be whittled away by judicial improvisation." *Clothing Workers* v. *Richman Bros.*, 348 U. S. 511, 514 (1955).

The District Court's injunction not only whittles away the statutory prohibition, but chops it right out of the law.

The ground of the District Court's decision was that counsel for respondents, the stockholder plaintiffs in this

derivative action, had a right to join in the negotiation of the settlement now under consideration in the State Court but had not been invited to do so. The equity of this settlement with regard to all parties is, however, precisely the question now being considered by the State Court referee, who has had the benefit of sixteen weeks of the fullest kind of hearing, after notice to all stockholders of Alleghany. It is anomalous for the District Court to admit, on the one hand, the right of the State Court to hear and determine all of the issues relating to the propriety and adequacy of the settlement and yet to conclude, on the other hand, upon motion papers alone, that the pending State Court decision should be entitled to no weight in the present action. Not only is this bar to pleading an admittedly valid judgment an altogether unique development in the law of *res judicata*, but it necessarily rests on the premise that the State Court cannot be relied upon to protect the stockholders of Alleghany from an inequitable settlement. Precisely the contrary policy underlies Section 2283:

> "The prohibition of § 2283 is but continuing evidence of confidence in the state courts, reinforced by a desire to avoid direct conflicts between state and federal courts." *Clothing Workers* v. *Richman Bros.*, 348 U. S. 511, 518 (1955).

The District Court's injunction also offends against the requirement of full faith and credit, which is made applicable in the federal courts by Section 1738 of the Judicial Code, 28 U.S.C.A. Sec. 1738. That Section requires the District Court to give the State Court judgment the same effect it would have in the State Court itself. In explaining the grounds for the issuance of the injunction, the District Court did not suggest that the State Court judgment would be subject to attack in the State Court on the same grounds. Nor was there any reason to believe the State Court would entertain such an attack on its judgment, since the fairness of the negotiations by which the settlement was arrived at are admittedly among the issues before the State Court in the settlement proceedings. And if there were any doubt on this score, it has since been laid to rest

in this very litigation by a recent decision of the Appellate Division, First Department, of the Supreme Court of the State of New York. That Court has ruled that the exclusion of respondents from the settlement negotiations does not *per se* vitiate the settlement.* Note, 65 Yale L. J. 543, *fn. 43* at 549. It follows *a fortiori* that a State Court judgment would not be subject to attack in the New York courts on the ground on which the District Court would deny it effect in the Federal Court. Surely the requirement of full faith and credit cannot be evaded by the simple device of announcing in advance the intention to violate it.

The rapidly developing and quantitatively very important field of stockholders' derivative litigation has received little attention from this Court in recent years. It is virtually standard practice in this type of litigation for plaintiffs to prosecute their actions simultaneously in both state and federal courts, *Brendle* v. *Smith*, 46 F. Supp. 522 (S. D. N. Y. 1942); thus giving rise to a serious likelihood of recurrence of situations analogous to the present one. Granting of the present petition will open the door for appellate consideration of broad questions of federal-state relations in the increasingly important field of stockholder litigation. Denial of the present petition may be expected to result in the destruction of the settlement and the invasion of state court jurisdiction by a federal court. Finally the door will be opened to variants on the injunction device which can seriously undermine full faith and credit and Section 2283 and can create abhorrent races and conflicts between state and federal courts.

In summary, petitioners urge these points:

1. The Court below patently misapplied the clear language of Section 1292(1) of the Judicial Code, so

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* "We construe the order of reference, in entitling appellant to raise any question as to the fairness, reasonableness or adequacy of the settlement, to include the issue of the effect, if any, of the exclusion of persons from the negotiations for settlement. We assume that *unless there is an adverse effect on the settlement by reason of such exclusion, exclusion will not have been shown to be improper.*" *Zenn* v. *Anzalone*, 1 App. Div. 2d 662, 146 N. Y. S. 2d 286, 287 (1st Dept. 1955) (emphasis added).

"as to call for an exercise of this Court's power of supervision."

2. The Court below acted in conflict with applicable decisions of this Court construing Sections 1292(1) and 1291 and may have applied decisions under Section 1292(1) which do not bear on the case at bar.
3. The action of the Court below, in deferring review of the District Court's order, left the way open for an improper invasion of the jurisdiction of the State Court which cannot be remedied by later appellate review.
4. The action of the Court below is likely to render moot substantial and novel questions regarding the proper functioning of the dual system of federal and state courts.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Dated: April 21, 1956.

Respectfully submitted,

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